U.S. House of Representatives
Committee on the Budget
B-71 Cannon House Office Building, Washington, DC 20515 (202) 226-7200 ★ democrats.budget.house.gov

Chris Van Hollen,
Ranking Democrat

Frequently Asked Questions About Sequestration Under the Budget Control Act of 2011

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1. **What did the Budget Control Act (BCA) do?**
The Budget Control Act of 2011 (P.L. 112-25) raised the statutory debt limit, narrowly avoiding a disastrous default on the public debt. At the same time, the BCA imposed annual limits on discretionary spending saving roughly $1 trillion over ten years, and created a Joint Select Committee on Deficit Reduction (the so-called "Supercommittee") tasked with finding at least an additional $1.2 trillion in deficit reduction. The law included a mandate for automatic spending cuts under sequestration as a last resort designed to encourage the Committee to find a bipartisan compromise for long-term deficit reduction.

2. **What is sequestration?**
A budget sequester requires the cancellation of budgetary resources, meaning that money that would otherwise be spent under current law is held back and used instead for deficit reduction.

Automatic Enforcement of the Joint Committee Target: The Deficit Reduction Sequester
The BCA triggers automatic enforcement procedures because the Joint Select Committee failed to reach agreement on at least $1.2 trillion in deficit reduction. That sequester consists of reductions taken equally from both the defense and non-defense sides of the budget. The first cuts from this sequester will take effect on January 2, 2013. In its report to Congress for the Sequester Transparency Act on September 14, 2012, the Office of Management and Budget (OMB) provided a listing of which accounts would be exempt and which would be cut as well as a rough estimate of how large a cut each category would face at that time.

Two other forms of sequestration enforce the annual discretionary caps and the Pay-As-You-Go rules,[1] but are not the focus of this report.

[1] **Discretionary Sequester.** If Congress exceeds any of the annual discretionary spending caps set by the BCA, then all non-exempt discretionary programs (but not mandatory spending) would be sequestered that year by an equal percentage sufficient to reduce total appropriations to the specified cap.

PAYGO Sequester. The Pay-As-You-Go Act of 2010 (PAYGO) reinstituted sequestration procedures to ensure that the total of all net new mandatory spending or tax cuts is offset by an equal amount of mandatory spending cuts or revenue increases. OMB keeps a scorecard tabulating all net costs and savings of legislation that change mandatory spending and revenues. At the end of the Congress, if the total shows net deficit reduction, there is no sequester. But if the net impact of mandatory and revenue legislation has worsened the deficit, then a PAYGO sequester of that amount is imposed on all non-exempt mandatory programs (but not on discretionary programs).

3. **How does the deficit reduction sequester work?**
The BCA requires spending cuts that will accomplish the deficit reduction that the Joint Select Committee on Deficit Reduction did not achieve. The cuts, to be carried out over a nine-year period, are divided evenly between defense and non-defense spending, including both discretionary and mandatory programs. The first round of cuts goes into effect on January 2, 2013.

4. **How much spending will the sequester cut?**
The deficit reduction sequester is designed to enforce savings of $1.2 trillion through 2021. For 2013, that means a $55 billion cut in defense and a $55 billion cut in non-defense spending. Based on the calculations in the law, spending on government programs will be reduced by $984 billion. The BCA envisions that the remaining savings will come from reduced debt service costs.

The Congressional Budget Office (CBO) has made rough calculations that the $984 billion in programmatic reductions will translate into $888 billion in deficit reduction through 2021. The deficit reduction amount is lower for two reasons. First, for discretionary programs the programmatic reduction applies to budget authority, which sets the level of funding a program is eligible to spend, but not how much actually flows out of the Treasury in that fiscal year. Changes in budget authority result in outlay changes – the actual flows from the Treasury – over a period of years. Some of the outlay changes from the sequester will occur beyond 2021 and are thus not included in the deficit reduction through 2021. Second, reductions in Medicare required under the sequester will have the effect of reducing Medicare premiums since they are calculated based on program costs. This lower income offsets a portion of the savings in the program.

5. **How much of the sequestration comes from discretionary versus mandatory spending?**
The bulk of the sequestration savings come from discretionary programs (those funded by annual appropriations bills) as opposed to mandatory programs (also known as direct spending, or entitlement spending, where the program's annual cost is generally determined by eligibility criteria established by law). The required savings are to come half from defense programs and half from non-defense programs. Within each half, the savings are allocated to discretionary and mandatory programs based on the contribution each makes to the total of discretionary budget authority and sequesterable direct spending. Because defense has almost no mandatory funding subject to sequestration, almost all of the defense portion will come from discretionary programs. On

2013 Deficit Reduction Sequester In billions of dollars			
	Defense	Non-Defense	Total
Discretionary	54.6	38.0	92.6
Mandatory	0.1	16.6	16.7
Total	54.7	54.7	109.3

Source: OMB.
Table may not add due to rounding.

the non-defense side of the budget, mandatory programs will account for about one-third of the non-defense savings because most mandatory spending is exempt. Thus, almost all defense savings and about two-thirds of non-defense savings will come from discretionary programs.

6. **What is the total effect on discretionary spending?**
   At the time of the BCA's enactment, CBO estimated that the initial discretionary spending caps cut spending by $800 billion over ten years (2012 through 2021) compared with continuing the current levels (which had already been reduced in previous legislation) adjusted for inflation. Those caps will now be replaced by even lower caps as part of the deficit reduction sequester. In its economic update this August, CBO estimated this will reduce discretionary spending by an additional $900 billion over ten years below the existing BCA caps. According to OMB's September 14 report, this provides $93 billion in savings for 2013.

7. **Which programs will be sequestered?**
   For 2013, the deficit reduction sequestration will apply individually to discretionary and mandatory programs unless they are specifically exempted. In its September 14 report, OMB provided a preliminary list of which accounts are exempt and approximately how much each category of spending will be cut.

   On the discretionary side of the budget, few accounts are exempted. Pell grants, spending from most transportation trust funds (which support highways, mass transit, and airports), and all programs administered by the Department of Veterans Affairs are exempt. The President also exercised his discretion to exempt military personnel accounts for 2013. While the pay rate and benefits for federal employees cannot be cut, agencies could furlough employees to achieve required savings.

   On the mandatory side of the budget, the bulk of spending is either exempt or subject to a special rule. Social Security is exempt, as are many programs that serve low-income beneficiaries, including Medicaid, Supplemental Nutrition Assistance Program (formerly called food stamps), Supplemental Security Income, and Temporary Assistance for Needy Families. Federal retirement and disability accounts and veterans' programs are exempted, as are most refundable tax credits. Other specific exemptions include a variety of government insurance programs and activities funded from private donations or voluntary contributions. Most of Medicare payments to providers are subject to sequestration but limited to a 2 percent reduction. (Some of Medicare is exempt and a small portion is subject to the full sequester.) Farm support programs comprise the largest component of the remaining mandatory spending subject to full sequestration.

For 2014 and beyond, the deficit reduction sequester works a little differently for discretionary programs. In those years, the discretionary sequester will lower the discretionary caps, not funding for individual programs. It will be up to the Appropriations Committee to determine how the cuts are allocated. If the Appropriations Committee breaches the caps, the separate discretionary sequester would apply at the account level to remove the breach.

8. **What are the firewalls? What is the "security" category?**
   The BCA sets different spending caps for different discretionary categories, separated by a "firewall" for enforcement purposes. If a cap is breached in one category, the firewall requires an offsetting sequester only within that portion of discretionary spending rather than across all discretionary categories.

   The BCA includes a security category that refers to programs within the federal budget's national defense function, which includes the Department of Defense, nuclear energy-related activities at the Department of Energy, the national security activities of several other agencies such as the Selective Service System, and portions of the activities of the Coast Guard and Federal Bureau of Investigation.[2]

9. **What percentage of the cut is in "defense" versus "non-defense" programs?**
   The deficit reduction sequester requires that half of the savings come from defense programs and half from non-defense programs.

10. **Is funding for Overseas Contingency Operations (OCO) exempt from a sequester?**
    No. Classification as OCO does not exempt spending from a sequester. However, to the extent that OCO funding is covered by other exemptions in the law, it will be exempt. The President has exempted military personnel from the sequester. As a result, the military personnel accounts classified as OCO will also be exempt.

11. **Will sequestration cuts be at the program level, or at the budget account level?**
    The upcoming deficit reduction sequestration occurs at the program-by-program level, with every non-exempt program cut by the percentage required to reach the calculated deficit reduction target for that year. There may be budgetary accounts within agencies that have some programs exempt from sequestration or where the size of the sequestration is limited by statute, whereas other programs are not exempt and are subject to the full cut required.

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[2] The security category for 2012 is defined differently. In addition to the Department of Defense, it includes the Departments of Homeland Security and Veterans Affairs, the National Nuclear Security Administration, the intelligence community management accounts, and accounts in the International Affairs function.

12. Who determines the size of the required cut, and when will we know the specifics?

Under budget law, OMB will manage all aspects of the deficit reduction sequester. The law specifies that OMB estimates are to be used to determine both which programs are exempt from the sequester and the size of the cut on the remaining programs. Neither the CBO nor the Budget Committees play a role in implementing the sequester. OMB issued a preliminary list of exempt programs and a rough estimate of the size of the cut to each category of spending in its September 14 report. OMB cannot calculate the precise cut to each program until after appropriations are enacted for 2013 and until it knows the level of unobligated balances in defense accounts at the time the sequester takes effect.

13. How much discretion does the President have in how the sequester is applied?

Almost none. The President does not have discretion to vary the size of the cut to agency budgets. The President has exercised his authority to exempt military personnel accounts from sequestration, which did not change the total defense sequester – the amount of the sequester on other defense programs will increase. All agencies will continue to have their existing transfer authority with the limitations that are specific to each agency.

14. How is the sequester in 2013 different from the sequester in following years?

The deficit reduction sequester for FY 2013 will reduce spending not only for all non-exempt mandatory programs, but it will also lower the amount already appropriated for all non-exempt discretionary programs. For FYs 2014 through 2021, the effect of the deficit reduction sequester on appropriations will be to lower the total annual discretionary cap. The Appropriations Committee will then allocate funding under that new, lower cap, but funding will not be further cut by a sequester (unless total appropriations exceed the caps set in law, in which case there will be a discretionary sequester). The sequester for mandatory programs for FYs 2014 through 2021 will follow the same process as for 2013.

15. Is there still time to prevent the deficit reduction sequester?

Yes, but only if Congress enacts legislation amending the BCA to turn off the sequester. For example, Congress could enact $1.2 trillion in deficit reduction but implement that savings in a different way than envisioned by the sequester.

16. Is there a waiver?

There is no waiver of the deficit reduction sequester unless there is a declaration of war. The only option for changing it would be to enact legislation to amend the BCA.

Sources for information mentioned in this report

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